STANDARD & POOR'S

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**Summary:**

# Oglethorpe Power Corp., Georgia; CP; Joint Criteria; Rural Electric Coop

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**Summary:**

# Oglethorpe Power Corp., Georgia; CP; Joint Criteria; Rural Electric Coop

| Credit Profile | | |
|---|---|---|
| US$300.00 mil 1st mtg bnds plant vogtle units 3 & 4 constr ser 2011A | | |
| *Long Term Rating* | A/Stable | New |
| **Appling Cnty Dev Auth, Georgia** | | |
| Oglethorpe Pwr Corp, Georgia | | |
| Appling Cnty Dev Auth (Oglethorpe Pwr Corp) poll cntl rev bnds (Oglethorpe Pwr Corp Hatch Proj) | | |
| *Long Term Rating* | A/Stable | Affirmed |
| **Burke Cnty Dev Auth, Georgia** | | |
| Oglethorpe Pwr Corp, Georgia | | |
| Burke Cnty Dev Auth (Oglethorpe Pwr Corp) | | |
| *Long Term Rating* | A/Stable | Affirmed |
| Burke Cnty Dev Auth (Oglethorpe Pwr Corp) poll cntl bnds (Oglethorpe Pwr Corp.) ser 2003A&B due 01/01/2024 | | |
| *Unenhanced Rating* | A(SPUR)/Stable | Affirmed |

## Rationale

Standard & Poor's Ratings Services has assigned its 'A' rating to Oglethorpe Power Corp. (OPC), Ga.'s $300 million first mortgage bonds, series 2011A, which the company expects to issue in the third quarter of 2011. Proceeds will fund a portion of the new Vogtle nuclear units' construction.

At the same time, Standard & Poor's affirmed its 'A' issuer credit rating on the utility, its 'A' rating on OPC's other long-term debt, and its 'A-1' rating on Oglethorpe's $1.3 billion commercial paper program. The outlook on the long-term ratings is stable.

The 'A' rating reflects our view of an above-average business profile score of '4' on Standard & Poor's 10-point scale, where '1' is the strongest. Oglethorpe, based in Tucker, Ga., is the largest generation cooperative in the U.S., It sells wholesale energy under take-or-pay contracts to 38 retail electric distribution cooperatives that serve portions of 151 counties throughout Georgia, including portions of suburban Atlanta. Oglethorpe has a total of 39 members, but one of those members is not set to begin receiving energy from OPC until 2016. Georgia Transmission Corp. (GTC; AA-/Stable/A-1+) provides transmission services to all 39 members. OPC's debt, which includes debt issued in the capital markets, lease obligations, and loans from the Federal Financing Bank (FFB), which the U.S. Department of Agriculture's Rural Utilities Service (RUS) guarantees, totaled $5.4 billion as of Dec. 31. 2010.

We believe credit strengths include the following:

- Strong take-or-pay contracts through 2050 for the sale of power, which provide for the joint and several obligation of Oglethorpe's member distribution cooperatives and step-up provisions in the event of default;
- Strong provisions for recovering energy costs, which the utility passes through to members on a 30-day lagged basis;

- A relatively modest reliance on volatile natural gas resources, at about 11% of its energy supply mix including purchases. However, since members source about 40% of their energy requirements, reliance on natural gas might be higher than OPC's portfolio suggests;
- The members' geographic and economic diversity;
- A principally residential customer base that accounts for about 70% of the member distribution cooperatives' revenues; and
- Oglethorpe's ability to set and adjust board-approved rates without regulatory oversight, coupled with a year-end adjustment mechanism to ensure full compliance with the company's minimum margin for interest (MFI) coverage of 1.1x.

We believe the following weaknesses temper these strengths:

- Increased business risks for the distribution cooperative members, given that all 39 members have chosen to procure incremental power from third-party power suppliers, which might increase the members' exposure to market and fuel volatility;
- A potentially weaker financial risk profile as the utility issues debt to fund the construction of its 30% share of the new nuclear units, Vogtle 3 and 4, which the owners expect will begin operating in 2016 and 2017, respectively; and
- Increased nuclear concentration if Vogtle 3 and 4 are built. In our opinion, the damage to several nuclear reactors in Japan from the earthquake and tsunami in March 2011 has had no effect on the credit quality of U.S. nuclear plant operators. However, this incident raises the probability of greater costs and oversight for existing nuclear plants located in the U.S. We expect that OPC would be able to recover any incremental costs from member cooperatives.

Oglethorpe was formed in 1974, and restructured into three companies in 1997. Initially a generation and transmission cooperative, it now owns only generation. OPC's large amount of base load capacity consists of undivided interests in facilities that were built by Georgia Power Co. (GPC; A/Stable/A-1) and are operated by GPC and Southern Nuclear Operating Co., both subsidiaries of The Southern Co. (A/Stable/A-1). Coal and uranium fuel the units, allowing the utility to provide power to its member cooperatives for a projected 6.5 cents per kilowatt-hour (kWh) in 2011, or about 7.2 cents including transmission plus the costs associated with generation facilities that Smarr Electric Membership Corp. (Smarr EMC; not rated) owns but Oglethorpe operates for the use of all members. The members' retail residential rates averaged 10 cents per kWh in 2010, which was in line with the state average. A pumped storage hydroelectric plant OPC operates helps offset the cost of the gas-fired peaking units that the utility owns. Oglethorpe expects wholesale prices to be competitive even after significant investment in equipment at the coal-fired plants to comply with environmental regulations. The rates will increase gradually thereafter to cover the investment in generating units. The cooperative board sets rates annually to assure compliance with the mortgage indenture requirement that MFI be at least 1.1x. The board voted to strengthen OPC's credit metrics during this period of construction, acquisition, and investment by raising the MFI to 1.12x in 2009 and 1.14x in both 2010 and 2011.

Oglethorpe supplied about 59% of the electricity member distribution cooperatives required in 2010. The power came from the 5,790 megawatts (MW) of owned and leased capacity, along with 562 MW of hydro power from the Southeastern Power Administration and 709 MW owned by Smarr EMC but managed by Oglethorpe. Under terms of the amended wholesale power contracts, members have the option of sourcing power needs beyond what they get from OPC resources through third-party suppliers. However, members will need additional base load capacity soon, and have agreed to participate in constructing two nuclear units at the Vogtle site. Oglethorpe and its members will own 30% of each unit, and their share of the cost is an estimated $4.2 billion (in 2008 dollars). By the end of 2011, the cooperative and its members will have invested about $1.4 billion for site preparation and purchase of some of the plant components. The Nuclear Regulatory Commission (NRC) issued the early site permit and limited work authorization in August 2009 and the NRC recently stated that it expects it to issue the construction permit and operating license in late 2011. OPC also acquired five combustion turbine units that supply power to some members, and in April 2011 bought two combined cycle units at a much lower cost than the combined cycle generating plant they'd planned to build.

Ahead of this building phase, management took steps to improve the utility's financial risk profile. Debt restructuring eliminated large, near-term bullet maturities and extended maturities of existing low-cost debt to provide borrowing capacity. The first step in this process was extending the maturity of the power sales contracts to 2050 from 2025, which management accomplished in 2005. In 2006, Oglethorpe refinanced pollution control bonds, extending maturities out to 2036-2041. It also issued taxable debt, primarily to fund the installation of environmental equipment at its Scherer plant. This was the first time in more than a decade that OPC had issued debt in the taxable 144A market, which provides a needed alternative source of financing. Traditionally, cooperatives have borrowed either directly from the RUS or from the FFB under an RUS guarantee. However, with the increasing need for generating capacity and requirements for emission controls, the amount of funding needed might exceed RUS's lending capacity, which Congress must approve each year. Finding alternative lenders will help ensure access to money needed for the capital investment. OPC was the first cooperative to take advantage of the opportunity to extend the maturity of RUS debt without repricing the issue, although it paid $4.6 million for modification costs. It extended about 20% of the RUS and FFB debt portfolio.

These refinancings and the FFB debt extension reduced annual principal payments to a level lower than annual plant depreciation. As a result, debt service coverage (DSC) in 2008 and 2009 improved to 1.35x. Fixed charge coverage, which includes purchased power capacity payments, lease payments and debt service, improved to 1.26x and 1.27x in 2008 and 2009, respectively. In 2010, DSC improved to 1.41x and fixed charge coverage to 1.34x.

We expect DSC to remain at 1.25x-1.30x during the construction period because of the board's commitment to keep MFI elevated if needed. If construction of the new units proceeds as planned, debt outstanding by 2017 will be about $9 billion, compared with $5.4 billion at the end of 2010, and debt service will be about $480 million, compared with about $310 million. Most, if not all, of the long-term debt funding the generating plant additions will have a fixed rate. The federal Department of Energy has indicated that it will provide a loan guarantee for up to 70% of the debt for the new nuclear units. The other 30% is being issued in the capital markets. This series 2011A first mortgage bonds will essentially complete the capital markets portion of the Vogtle financing.

Oglethorpe's highly leveraged capital structure is typical of generation and transmission cooperatives. At the member level, debt is generally about 55% of total capital. But the members' ability to honor the terms of their take-or-pay power sales contracts establishes the basis of our evaluation of OPC's credit strength. Under the contract terms, the members must make payments sufficient to cover all costs, including debt service, plus a margin for interest. That commitment implies an unlimited step-up should any member default.

We believe Oglethorpe's liquidity position is very strong, and management has taken steps to increase available liquidity during the construction period. In addition to cash on hand, which is targeted at $400 million-$600 million, OPC has a $1.3 billion liquidity facility that matures in July 2015. The facility backs a $1.3 billion commercial paper program and also allows direct borrowing and up to $500 million in letters of credit. The utility also has four credit facilities totaling $600 million for general working capital purposes. The National Rural Utilities Cooperative Finance Corp. and CoBank ACB, both cooperative lending institutions, and JPMorgan Chase Bank provide these lines. Oglethorpe's actual operating liquidity requirements are moderate, in our view. Commodity price risk is limited because natural gas costs are passed through to members with a monthly true-up.

## Outlook

The stable outlook reflects our view of the board's stated commitment to maintain a financial risk profile appropriate for the ratings as management adds substantial generating assets. These plans will likely increase OPC's debt to about $9.0 billion by 2017 from $5.4 billion currently, and debt service will increase about 50%. In accordance with the indenture, Oglethorpe must set wholesale rates high enough to cover costs plus an MFI of 1.10x. The board raised the MFI to 1.14x for 2010 and 2011, which translates into a DSC ratio of 1.25x-1.30x. The board also directed management to increase liquidity significantly. We view both of these steps as evidence of its commitment to a moderately strong financial risk profile.

## Related Criteria And Research

USPF Criteria: Applying Key Rating Factors To U.S. Cooperative Utilities, Nov. 21, 2007

| **Ratings Detail** (As Of August 11, 2011) | | |
|---|---|---|
| Oglethorpe Pwr Corp | | |
| *Long Term Rating* | A/Stable | Affirmed |
| Oglethorpe Pwr Corp ICR due 05/13/2055 | | |
| *Long Term Rating* | A/Stable | Affirmed |
| Oglethorpe Pwr Corp 4(2) CP | | |
| *Short Term Rating* | A-1 | Affirmed |
| **Oglethorpe Pwr Corp 1st mtg** | | |
| *Unenhanced Rating* | A(SPUR)/Stable | Affirmed |
| **Burke Cnty Dev Auth, Georgia** | | |
| Oglethorpe Pwr Corp, Georgia | | |
| Burke Cnty Dev Auth (Oglethorpe Pwr Corp) poll cntl rev bnds (Oglethorpe Pwr Corp) (Oglethorpe Pwr Corp Vogtle Proj) ser 2010A due 01/01/2037 | | |
| *Long Term Rating* | AAA/A-1 | Affirmed |
| *Unenhanced Rating* | A(SPUR)/Stable | Affirmed |
| Burke Cnty Dev Auth (Oglethorpe Pwr Corp) poll cntl rev bnds (Oglethorpe Pwr Corp) (Oglethorpe Pwr Corp Vogtle Proj) ser 2010B due 01/01/2037 | | |
| *Long Term Rating* | AAA/A-1 | Affirmed |
| *Unenhanced Rating* | A(SPUR)/Stable | Affirmed |
| Burke Cnty Dev Auth (Oglethorpe Pwr Corp) poll cntl rev bnds (Oglethorpe Pwr Corp Vogtle Proj) ser 2004 due 01/01/2020 (AGM) | | |
| *Unenhanced Rating* | A(SPUR)/Stable | Affirmed |
| **Burke Cnty Dev Auth (Oglethorpe Pwr Corp) poll cntl** | | |
| *Unenhanced Rating* | A(SPUR)/Stable | Affirmed |

| **Ratings Detail** (As Of August 11, 2011) **(cont.)** | | |
|---|---|---|
| **Heard Cnty Dev Auth, Georgia** | | |
| Oglethorpe Pwr Corp, Georgia | | |
| Heard Cnty Dev Auth (Oglethorpe Power Corporation) GO VRDO ser 2009A | | |
| *Long Term Rating* | AAA/A-1+ | Affirmed |
| *Unenhanced Rating* | A(SPUR)/Stable | Affirmed |
| Heard Cnty Dev Auth (Oglethorpe Pwr Corp) poll cntl bnds (Oglethorpe Pwr Corp.) ser 2003A due 01/01/2024 | | |
| *Unenhanced Rating* | A(SPUR)/Stable | Affirmed |
| **Monroe Cnty Dev Auth, Georgia** | | |
| Oglethorpe Pwr Corp, Georgia | | |
| Monroe Cnty Dev Auth (Oglethorpe Pwr Corp) | | |
| *Long Term Rating* | A/Stable | Affirmed |
| Monroe Cnty Dev Auth (Oglethorpe Pwr Corp) poll cntl rev bnds (Oglethorpe Pwr Corp) (Oglethorpe Pwr Corp Sherer Proj) ser 2010A due 01/01/2036 | | |
| *Long Term Rating* | AAA/A-1 | Affirmed |
| *Unenhanced Rating* | A(SPUR)/Stable | Affirmed |
| Monroe Cnty Dev Auth (Oglethorpe Pwr Corp) GO VRDO ser 2009A&B | | |
| *Long Term Rating* | AAA/A-1+ | Affirmed |
| *Unenhanced Rating* | A(SPUR)/Stable | Affirmed |
| Monroe Cnty Dev Auth (Oglethorpe Pwr Corp) poll cntl bnds (Oglethorpe Pwr Corp.) ser 2003A due 01/01/2024 | | |
| *Unenhanced Rating* | A(SPUR)/Stable | Affirmed |
| Monroe Cnty Dev Auth (Oglethorpe Pwr Corp) poll cntl rev bnds (Oglethorpe Pwr Corp Scherer Proj) ser 2004 due 01/01/2020 (AGM) | | |
| *Unenhanced Rating* | A(SPUR)/Stable | Affirmed |

Many issues are enhanced by bond insurance.

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